



Oklahoma Economic Report™

News and analysis of Oklahoma's economy

A publication of the Office of the State Treasurer • Treasurer Ken Miller, Ph.D.

State's financial team promotes Oklahoma

A delegation of state officials are just back from a trip to the world's financial center where they gave credit ratings agencies the remarkable story of Oklahoma's economic strength and progress in improving its fiscal position.

On last week's trip were Governor Mary Fallin, State Treasurer Ken Miller, Secretary of Finance Preston Doerflinger and State Bond Advisor Jim Joseph.

"Our meetings with the leading credit ratings agencies in New York were an important opportunity to showcase Oklahoma's sound fiscal policies, strong economy and impressive job growth," said Fallin.

"Along with Treasurer Miller and Secretary Doerflinger – our fiscal 'A-Team' – we made the case that these factors make Oklahoma a great place to invest. The message the ratings agencies heard from us was that unlike the federal government, Oklahoma has a balanced budget and is making government smaller, smarter and more efficient."

In the meetings with Moody's, Fitch and Standard & Poor's, Fallin championed the Oklahoma success story. She touted the state's top national rankings for entrepreneurial activity and income, productivity and employment growth.

"... Oklahoma has a balanced budget and is making government smaller, smarter and more efficient."

Fallin highlighted other positive growth factors like the state's favorable business climate, low cost of living and high quality of life. She also presented

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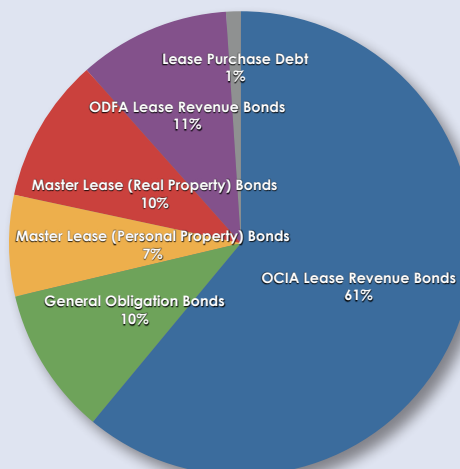
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Oklahoma Tax-Supported Debt

Debt service as percentage of General Fund Appropriations: 4.03%



Gross and Net Tax-Supported Debt (in millions)

OCIA Lease Revenue Bonds	\$1,322.7
General Obligation Bonds	\$223.1
Master Lease (Personal Property) Bonds	\$152.8
Master Lease (Real Property) Bonds	\$218.2
ODFA Lease Revenue Bonds	\$228.7
Lease Purchase Debt	\$22.4
Total Gross Tax-Supported Debt	\$2,168.0
Self-Supporting Bonds and Debt Service Reserve Funds	-\$123.3
Net Tax-Supported Debt	\$2,044.6

Source: Oklahoma State Bond Advisor, 2010 Annual Report



Treasurer's Commentary By Ken Miller, Ph.D.



Taxes, incentives and spending . . . oh my!

Numerous surveys show the vast majority of Oklahomans believe our state is moving in the right direction. The yellow brick road the state is traveling has been paved by a hard-working people, abundant natural resources and a pioneering spirit.

With nearly unparalleled growth in employment, migration, productivity, and per capita income, even the naysayer can recognize our state is navigating well through the economic forest.

As we near the upcoming legislative session, a sense of optimism pervades thanks to the progress made this interim on fiscal policy and the renewed interest in reforming a less than optimal tax code.

While there has already been a great deal of focus on taxes and incentives, government spending will soon move to center stage.

Taxes, incentives and spending are like a three-legged stool and sound fiscal policy dictates that each be considered in tandem. One cannot draw a conclusion on revenue sufficiency without addressing the spending side of the equation.

Of course, either side of that simple equation can lead to endless debate. The path becomes clearer when economics, rather than politics, guide the decisions surrounding each of the three.

“Many would agree taxes need to be lower, broader, fairer and flatter. Far fewer agree on how to get there.”

As the discussion evolves, the following considerations should be included:

Taxes

The ideal tax and fee structure would generate a predictable, stable and diversified revenue stream that sufficiently funds core government services without harming the profit motive that drives entrepreneurship, productivity and growth.

Many would agree taxes need to be lower, broader, fairer and flatter. Far fewer agree on how to get there. However, simply tinkering around the edges of the existing tax code seems

insufficient to adequately modernize an outdated system.

Incentives

Because state-backed credits, exemptions and deductions are just another form of spending, decisions regarding such incentives should be made on a cost-versus-benefits basis.

If the return on investment is positive in terms of jobs, income growth or infrastructure development, the incentive should be maintained. If not, the incentive should be terminated.

All incentives should meet the three-way test of public purpose, consideration and control as well as have expiration dates and maximum transparency.

Spending

Just as with incentives, state appropriations should be based on a cost-versus-benefit analysis.

Although efficiencies have been gained through government modernization efforts, opportunity still exists to better prioritize the

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Commentary

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budget so funds are directed into areas of highest return on investment.

By eliminating nonessential spending and ineffective incentives and broadening the revenue base, a new tax structure can emerge that both lowers rates and supports the private sector by properly funding core government responsibilities.

At times it is difficult to stay on the path and see the forest for the trees.

Like most years, this legislative session will be filled with distracting lions and tigers and bears.

But equipped with the courage to make tough decisions, a heart for our most disadvantaged and the brains to choose long-term growth over short-term expediency, Oklahoma's capable leaders can modernize our tax and spend policy to better serve our citizens.

Financial team

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legislative successes and goals for the upcoming session.

Miller reviewed the state's current economic indicators and reported on progress in areas previously identified by ratings agencies as weaknesses, including the state's pension liabilities.

Doerflinger reported on general revenue fund growth and efficiencies gained from government modernization and consolidation initiatives.

Joseph provided details on bond indebtedness, repayment schedules and potential bond issuances.

At a time when many states are still struggling through a slow economic recovery, Miller said it was refreshing to share all the good news coming out of Oklahoma.

"The shining state on the prairie has a very positive story to tell," said Miller. "We've managed through the recession better than most states by maintaining core services without a tax increase.

"We are replenishing our rainy day fund, addressing our pension problems and have responsible levels of debt."

He said obtaining a AAA bond rating is a long-term goal that would equate to an even lower cost of debt. But he also noted the state's current rating is strong and the last bond issuance, the OCIA's \$70 million State Highway Capital Improvement bond, secured a true interest cost of 2.2 percent over the 14-year term.

Several states – most recently Connecticut – have seen ratings or outlooks downgraded.

In contrast, Miller said Oklahoma is well-positioned to receive an upgrade in its outlook and perhaps a rating increase from Moody's, which has assigned Oklahoma a slightly lower score than the other two agencies.

Oklahoma currently holds the second-highest available rating, an AA+ from both Standard & Poor's and Fitch, and an AA2 from Moody's – that agency's third-highest rating. A rating of AAA indicates sterling credit, but any upgrade

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Comparing Oklahoma to States with Similar Bond Ratings

State	Rating			2009	2010	2010	Nov 2011		2010	2010
	Moody's	S&P	Fitch	Fed spending % state oper rev	Net Tax Supported Debt % Personal Income	Net Tax- Supported Debt per Capita (\$)	Unemployment Rate (%)	Population Change 2000-2010 (%)	Per Capita Income as % of U.S. (2000 Census)	Unavail Fund Bal + Reserves % Total Operating Revenues
Michigan	Aa2	AA-	AA-	0.4%	2.20%	\$766	9.8%	-0.72%	102.7%	1%
Massachusetts	Aa1	AA+	AA+	0.3%	9.40%	\$4,772	7.0%	2.92%	120.2%	8%
Minnesota	Aa1	AA+	AA+	0.3%	2.70%	\$1,156	5.9%	7.50%	107.5%	-10%
New Mexico	Aaa	AA+	-	0.5%	5.60%	\$1,805	6.5%	13.04%	80.0%	6%
Ohio	Aa1	AA+	AA+	0.6%	2.80%	\$1,006	8.5%	1.52%	97.3%	-1%
Oklahoma	Aa2	AA+	AA+	0.5%	1.80%	\$629	6.1%	8.61%	81.7%	24%
Oregon	Aa1	AA+	AA+	0.6%	5.60%	\$2,019	9.1%	11.67%	97.0%	-7%
South Carolina	Aaa	AA+	AAA	0.8%	2.80%	\$881	9.9%	14.96%	87.1%	1%
Tennessee	Aaa	AA+	AAA	0.5%	1.00%	\$344	9.1%	11.28%	89.8%	4%
Texas	Aaa	AA+	AAA	0.5%	1.70%	\$614	8.1%	20.03%	90.9%	7%
Vermont	Aaa	AA+	AAA	0.3%	1.90%	\$743	5.3%	2.59%	95.5%	8%
Washington	Aa1	AA+	AA+	0.5%	6.30%	\$2,634	8.7%	13.76%	106.4%	-4%
Overall average				0.5%	3.65%	\$1,447	7.8%	8.90%	96.0%	3%

Above average
Below average

Source: JPMorgan Chase & Co



December by the numbers: Gross receipts vs. General Revenue Fund

A comparison of the Treasurer's January 4 Gross Revenue Report and State Finance's January 10 General Revenue Fund (GRF) report illustrates fundamental differences.

December gross receipts totaled \$960.8 million, while the GRF received \$542.4 million or 56.5% of the total. Last month, the GRF received 52.8% of the gross.

The GRF received between 35% and 58% of monthly gross receipts during 2011, highlighting the value of using total collections rather than the GRF subset to gauge state economic performance.

From gross receipts in December, the GRF received:

- Personal income tax: 74.3%
- Corporate income tax: 58.9%
- Sales tax: 44.5%
- Gross production-Gas: 80.8%
- Gross production-Oil: 73.2%
- Motor vehicle tax: 32.6%
- Other sources: 46.5%

GRF collections for the month topped the official estimate by \$77.4 million or 16.6 percent.

Insurance premium taxes totaled \$36.1 million in December.

Tribal gaming fees generated \$10.2 million during the month.

2011 brought improved economic health to Oklahoma

Oklahoma's economy quickened the pace of its recovery during 2011, State Treasurer Ken Miller said upon release of the state's monthly gross receipts report.

"December was 11.1 percent better than the prior year, the fourth quarter was 10.5 percent ahead of the final three months of 2010, and total year collections surpassed the previous year by 9.6 percent," Miller said. "We saw healthy growth each month ranging from four to 16 percent with an average at the double-digit mark."

Miller said December was the fifth time in the past eight months that collections rose by more than 10 percent over the prior year and marked the 22nd consecutive month of growth.

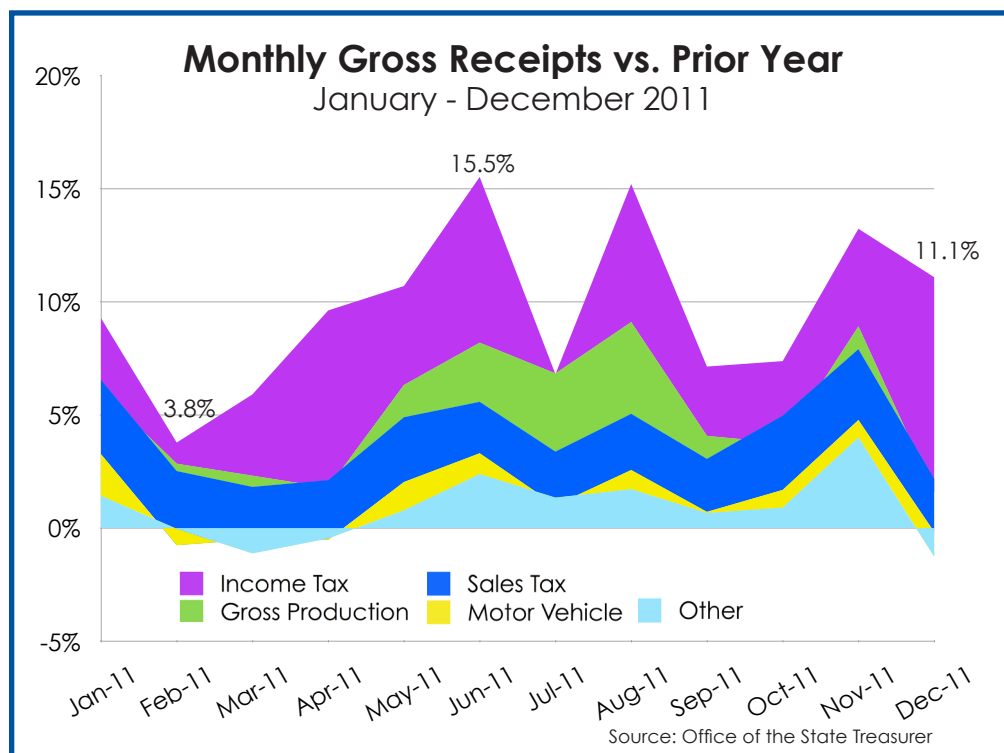
"Twelve-month collections now stand more than \$1.3 billion higher than in February of 2010. Since we hit the trough almost two years ago, more than 68 percent of the revenue lost from our peak in December 2008 has been recovered," he said.

Miller said sales tax collections indicate a happy holiday shopping season in Oklahoma. December collections, reflecting sales between mid-November and mid-December, were \$20.42 million or 6.3 percent higher than the last Christmas shopping season.

Looking forward

National and state-specific forecasts point toward continued economic improvement.

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Revenue

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Recent Bureau of Labor Statistics data list Oklahoma with year-over-year employment growth of three percent, surpassing all surrounding states. The closest competitor was Texas with growth of 2.2 percent.

A U.S. Chamber of Commerce report shows Oklahoma with the nation's fourth lowest unemployment rate, adding jobs 3.5 times faster than the national rate in 2011.

During the past 12 months, figures from the Oklahoma Employment Security Commission and Bureau of Labor Statistics show the labor force grew by just more than 15,000.

During that time, the unemployment rate dropped from 6.8 percent to 6.1 percent.

Oklahoma jobless rate unchanged

Oklahoma's unemployment rate held steady at 6.1 percent in December according to preliminary figures released January 24 by the Federal Bureau of Labor Statistics and Oklahoma Employment Security Commission.

December's rate is 0.7 percentage points less than the rate of 6.8 percent in December 2010.

The seasonally-adjusted figures show Oklahoma added 41,600 non-farm jobs in the past 12 months.

The state unemployment rate has been set at 6.1 percent since October.

Miller names Chief Deputy Treasurer

State Treasurer Ken Miller has announced the promotion of Susan Nicewander to the position of Chief Deputy Treasurer effective January 1. Nicewander previously served as Deputy Treasurer for Operations.

"Throughout the tenure of three treasurers, Susan has maintained the highest level of professionalism and ethical standards," Miller said.

"Well-liked and respected by her peers and colleagues, no one is more deserving of this key post. The citizens

of Oklahoma are fortunate to have such a dedicated and trustworthy public servant."

Prior to assuming responsibility for operations in 2007, Nicewander spent 11 years as the Internal Auditor for the Office of the State Treasurer. From 1988 to 1996, she served as City Auditor for Oklahoma City. She also has experience in the private sector.

Nicewander is a certified public accountant and holds an accounting degree from Oklahoma State University.

General revenue tops estimate

Allocations to the General Revenue Fund (GRF) for the first half of Fiscal Year 2012 are higher than the estimate, according to the Office of State Finance.

GRF allocations for the July-December period total \$2.698 billion, which is \$239.1 million or 9.7 percent higher than the estimate.

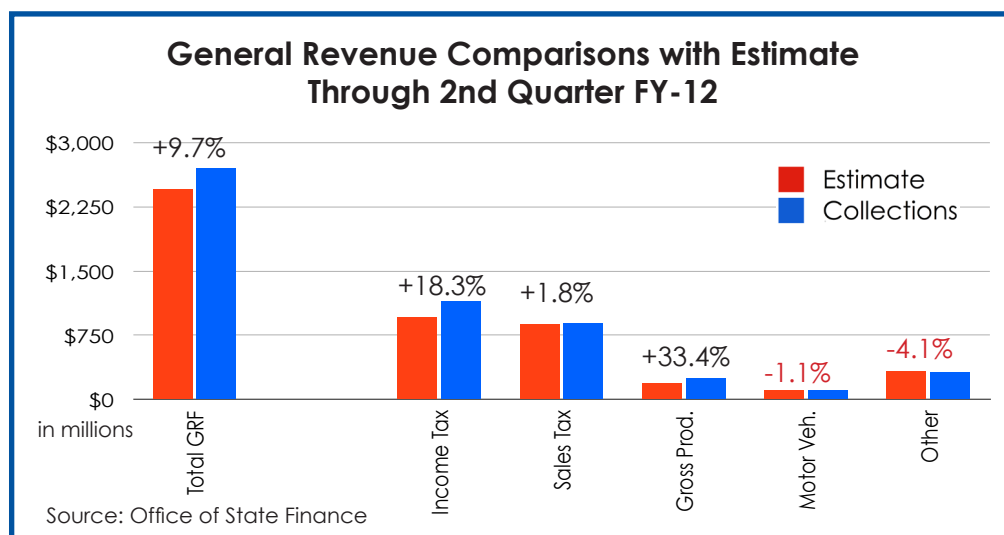
Net income taxes top the estimate by \$176.4 million or 18.3 percent.

Sales taxes exceeding the estimate by \$15.8 million or 1.8 percent.

The gross production tax is \$61.6 million or 33.4 percent above the estimate.

Motor vehicle taxes fell below the estimate by \$1.2 million or 1.1 percent.

Other sources are \$13.4 million or 4.1 percent less than the estimate.





Financial team

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would result in Oklahoma receiving its highest-ever credit rating.

In determining a state's credit worthiness, ratings agencies typically evaluate institutional framework, including fiscal policy structures; financial management of the state budget; economic variables, such as demographics and economic development policies; and a state's debt burden, including pension liabilities.

Each ratings agency mentioned two areas that have historically had a negative impact on Oklahoma's bond rating: a constitutional constraint on raising taxes and the state's unfunded pension liabilities.

Miller said he and the governor both expressed support for the restriction on raising taxes believing it to be sound fiscal policy.

"The restriction has helped constrain state government spending and has forced cost-cutting solutions and efficiencies that may not have come

about had revenue-raising been easy," he said.

State Question 640, approved by voters in 1990, requires revenue-raising measures either be approved by a vote of the people or by three-fourths of the Legislature. Regardless of how fiscally prudent it may be, Miller said the ratings agencies consider it one less arrow in the state's quiver.

Miller agreed the state's pension liabilities are a legitimate source of concern.

However, he updated the ratings agencies on reforms enacted during the 2011 legislative session that reduced the collective unfunded liability of the state's pension system by \$5.5 billion; news that he said received a very positive reaction from ratings officials.

Also well-received was information provided by Joseph on Oklahoma's debt holdings and repayment schedule.

Joseph said Oklahoma's per capita debt is just over one percent of 2010 per capita personal income and four percent of General Revenue Fund appropriations. Information presented to the ratings agencies demonstrated Oklahoma is on track to have 93.4

percent of outstanding tax-supported bond debt repaid within 20 years.

Joseph said Oklahoma is taking advantage of the favorable interest rate environment to refinance state-held debt, and he projected combined savings of close to \$30 million from transactions completed in 2011 through the end of this month.

Meeting participants complimented Oklahoma on its nearly unparalleled retail participation by state citizen investment in state-backed bonds, attributing that to Oklahoma's good track record of repayment and the fact that it doesn't issue much debt.

Miller said the meetings were a great opportunity to highlight the state's commitment to addressing future needs in a fiscally responsible way.

"The Governor made a great impression in New York and represented Oklahoma very well. She drew attention to the many areas deserving of consideration when ratings agencies evaluate Oklahoma's bond ratings and economic outlook," he said.

"The end result could ensure more taxpayer dollars are spent on investments and less on interest."

Economic News Briefs

China Trade

The U.S. trade deficit with China was around \$300 billion last year.

Each iPad sold in America adds \$275 to the deficit with China, because they are assembled in China. Since most of the parts come from outside China, the value added by assembly is only \$10. If Chinese exports to the U.S. were

calculated on a value-added basis, the deficit would be only \$150 billion.

Since Apple's profit is about 30% of the price, most of the benefits of selling iPads accrue to American shareholders and workers. Add in American suppliers and distributors and one-half of the total value of an iPad sold here is retained by Americans.

European Debt

S&P downgraded the long-term ratings of nine countries this month, including France and Austria to AA+ from AAA. This could affect the rating of the European Financial Stability Facility, the eurozone bailout fund.

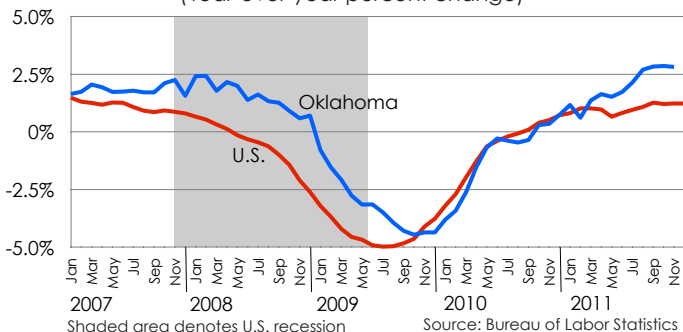
Reprinted from Baird Fixed Income Commentary, January 17 & 23, 2012



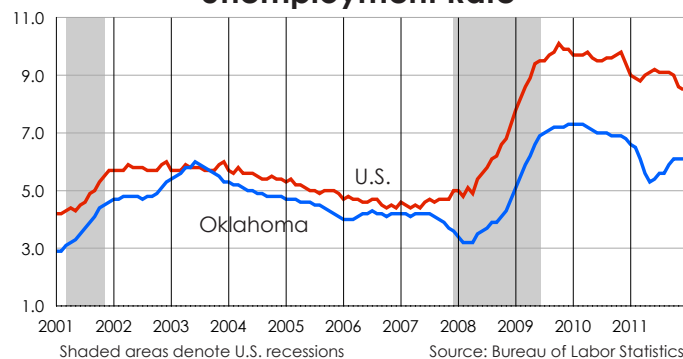
Economic Indicators

Job Growth

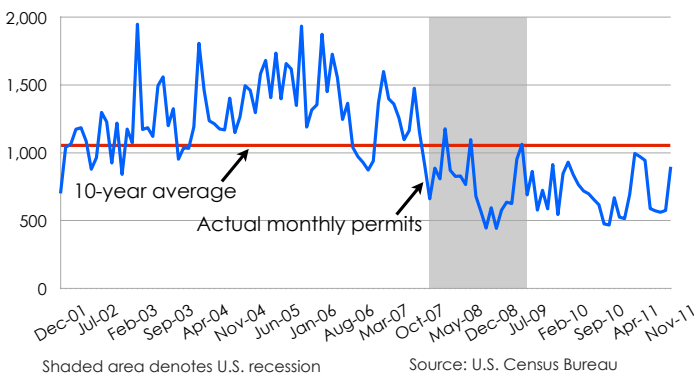
(Year-over-year percent change)



Unemployment Rate

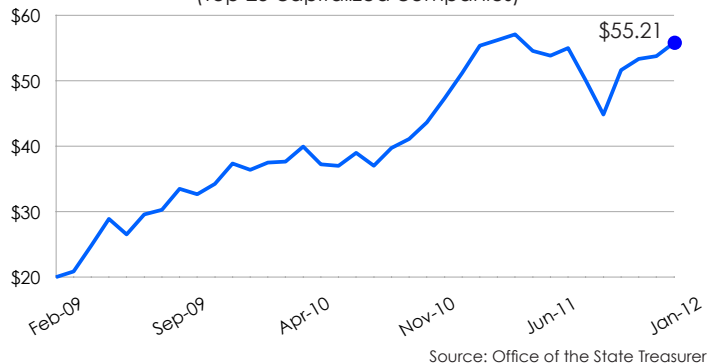


Oklahoma Residential Building Permits



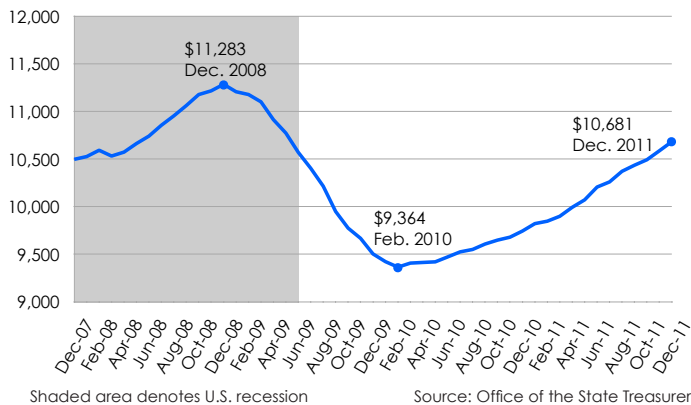
Oklahoma Stock Index

(Top 25 capitalized companies)



Oklahoma 12-Month Gross Receipts

December 2007 - December 2011
Dollars (in millions)



Oklahoma Active Rigs vs. Oil Prices

